Vietnam: Revolving credit fund for self-help oriented poverty reduction III

Ex post evaluation report

OECD sector	24030 – Formal sector financial intermediaries	
BMZ project IDs	1998 65 668	
Project executing agency	Ministry of Labour, War Invalids and Social Affairs (MOLISA) Vietnam Bank for Agriculture and Rural Development (VBARD)	
Consultant	Not applicable	
Year of ex post evaluation	**2006**	
	Project appraisal (planned)	**Ex post evaluation (actual)**
Start of implementation	01/2002	01/2002
Period of implementation	24 months	20 months
Investment costs	No information available	No information available
Counterpart contribution	No information available	No information available
Financing, of which Financial Cooperation (FC) funds	EUR 5.1 million	EUR 5.1 million
Other institutions/donors involved	None	None
Performance (overall rating)	3	
• **Significance / relevance (sub-rating)**	3	
• **Effectiveness (sub-rating)**	3	
• **Efficiency (sub-rating)**	4	

Brief description, overall objective and project objectives with indicators

The overall project objective was to reduce poverty in the programme region. The programme objective was the broad-scale award of small short-term, medium-term and long-term loans at market conditions to economically active poor rural households. The programme region comprises five rural provinces within the rice growing region in the Red River delta. FC funds amounting to EUR 5.1 million were made available to the Vietnam Bank for Agriculture and Rural Development (VBARD) as a revolving credit fund.

Programme design / major deviations from the original programme planning and their main causes

TheMinistry of Labour, War Invalids and Social Affairs (MOLISA) is still lead-managing poverty reduction projects and, in accordance with Vietnamese wishes, acts as the recipient of the funds. MOLISA has an administrative substructure, which extends from the provincial level (DOLISA) to the municipal level. As part of the project, MOLISA's task was to select the provinces as well as the districts and municipalities within the provinces. MOLISA was also mandated to identify potential target groups within the programme region on the basis of the incidence of poverty and to nominate potential borrowers for VBARD. MOLISA has carried out these tasks satisfactorily. The autonomy of VBARD agreed at the time of the project appraisal with regard to lending decisions was confirmed numerous times vis-à-vis the evaluation mission of MOLISA and VBARD, However, it cannot be entirely ruled out that DOLISA and the People's Committees will bring influence to bear on lending decisions at the local level.

VBARD, which was established in 1988, has existed since 1990 as a financial institution which is economically separate from the State Bank of Vietnam (SBV). VBARD is wholly owned by the state and is subject to direct supervision by the SBV. Since 1996 it has focused particularly on its work on the "development of the rural economy". In the rural areas VBARD is the main financial institution. It therefore also continues to serve as an important government instrument in the field of poverty reduction in the rural regions. In contrast to the other state commercial banks (SOCB), there are so far no actual indications or plans with regard to privatisation or partial privatisation of VBARD.

In recent years VBARD has received extensive technical support (including from the Asian Development Bank and the World Bank) and has actually been in a restructuring process since 2001. However, this restructuring process has not always been straightforward and consistent. In addition to improvements in the organisational and operational structure (e.g. prompt transfer of information between branches and the head office by online connections), the main very positive developments since the project appraisal are the physical separation of VBARD from the Bank for Social Policy (formerly Bank for the Poor) and the greater transparency in the publication of the annual financial statements. From the point of view of transparency, we consider it positive that for some five years VBARD has been consistently publishing annual financial statements on the basis of international accounting standards. Overall, the pace of reform seems to be gaining momentum owing to clear political requirements since 2004 and the opening-up of the banking sector expected to result from Vietnam's efforts to become a member of the WTO.

The Socialist Republic of Vietnam, represented by the Ministry of Labour, War Invalids and Social Affairs (MOLISA), was the recipient of the FC grant of EUR 5.1 million. The FC funds were forwarded to VBARD as the project executing agency in the domestic currency with a term of 15 years and were used to set up a revolving credit fund of VND 75.7 billion (EUR 5.1 million at the time of disbursement). The exchange rate risk was borne by the Ministry of Finance, which we consider appropriate. The refinancing rate for VBARD was to be set as a variable rate dependent on the level of the sub-loan interest rate less a bank margin of 9%. The sub-loans should be granted at market-based interest rates. Return flows to the bank from repayments of the sub-loans are to be used for a further lending. The at A maximum of three years was set as the term for the sub-loans and the maximum amount of the loans used for financing investment capital and working capital was fixed at VND 5 million at the time of the project appraisal. By virtue of its letter dated 29 July 2003, the BMZ raised the upper credit limit to VND 7 million and on 29 November 2005 to VND 10 million. We consider that appropriate. The loans are to be granted in accordance with the graduated principle, i.e. the first loan may not exceed 60% of the maximum amount. If repayment functions successfully, the amount goes up to 80% and, in the third round, to 100% of the maximum amount. The default risk for the sub-loans is borne by VBARD and the Bank must make up for ultimate loan losses from its own resources (requirement). Actual repayments of the loans were relatively close to 100%. As part of the FC project, the cooperation between VABRD and the Women's Union ("retail lender") with regard to the granting of sub-loans proved very worthwhile. The interest differential funds are accumulated on a counterpart fund account and are used primarily to retain the real value of the revolving credit fund (inflation compensation).

At the time of the ex post evaluation, 60,136 loans with a total volume of VND 245.7 billion (approximately EUR 11.9 million) had been granted. The fund has thus revolved 3.2 times since the start of the project. Most of the loans had a maturity of more than two years and were granted to finance investment capital (Annex 6). The average loan is for VND 4.1 million or EUR 198. More than 90% of the loans were channelled to agriculture (including fishing), primarily for animal husbandry (70% of all loans). The distribution of loans by province puts Nam Dinh in the lead with 40%, followed by Thanh Hoa and Thai Binh with 20% each. Around 39% of the borrowers were women. A positive assessment is given of the rapid execution of the programme (20 months after the due disbursement date, all funds had been disbursed in first-round loans).

The random checks of loan files and visits to the borrowers showed that the above-mentioned conditions were observed. The on-site review of the books to check how the funds were used provided no indication of misuse of funds.

Key results of the impact analysis and performance rating

The programme aimed at broad-based granting of small short, medium and long-term loans at market conditions to economically active poor rural households whose income is not sufficient to allow them to make small investments.

The achievement of the programme objectives was to be measured in 2005 at the earliest using the following indicators: (a) gross loan portfolio of the revolving fund is more than or equal to EUR 5.1 million (real capital value); (b) share in the total loan portfolio of loans with interest and/or principal arrears of over 90 days is less than or equal to 5%; (c) share of restructured loans in the FC programme is less than or equal to 10%; (d) average amount of loan is less than or equal to EUR 306; (e) the programme has reached at least 20,000 poor loan applicants.

At the time of the ex post evaluation, indicator (a) had not been met, as the VND had depreciated considerably vis-à-vis the euro (at the time of the ex post evaluation, real value of the fund: EUR 3.9 million). Even if the (more appropriate) indicator of the real value in VND is used, compared with the original fund volume of VND 75.7 billion there has been an inflation-induced loss in real value. This is, in particular, because, in accordance with the agreement, only repayments to the revolving fund are recorded and not interest payments. Even at very good repayment rates, inflation causes a fund structured in this manner to lose real value. To offset this loss, MOLISA has paid VND 7.3 billion from the counterpart resources fund into the loan fund. Taking account of this payment, the real value of the loan fund in relation to the time of the project appraisal is VND 70.1 billion. According to information from VBARD, the indicators (b) and (c) were met, at 0.24% and 1.15% respectively. Taking account of the restrictions regarding the quality of the portfolio in the auditors certificates issued by PWC for the VBARD annual financial statement 2004 and the random samples taken by the evaluation mission at VBARD branches, the values do not, however, appear very informative. The level of the actual portfolio at risk cannot be determined as it is apparently VBARD practice in the FC project not to settle interest rate payments and repayments of the principal until the end of the loan term. The indicators (d) and (e) have been very clearly met with the average loan being EUR 198 and more than 60,000 loans granted. Overall, we judge the programme objectives to have been achieved to a just sufficient degree.

By improving access to financial services, the programme aims at reducing poverty in the programme region (overall objective). The overall objective was to be deemed to have been reached if (a) the net budget income of the end-borrowers has increased in relation to the control group outside the programme region and (b) low-income population groups have improved access to financial services provided by formal financial institutions. Indicator (a) was adjusted in accordance with the progress review 12/2005 in that a “before” and “after” comparison was to be made rather than a comparison with a control group.

At the time of the ex post evaluation there was no empirical study on the income effects of the FC project on the target group. Moreover, MOLISA has no initial data on the target group at the time when the project started (baseline survey). Subsequent collection of data would be time-consuming and expensive as well as problematic in terms of methodology and because of the lack of initial data. It therefore appeared to be more appropriate to select easily collected proxi-indicators, such as the poverty rate in the programme regions, as the provincial governments have these figures for individual districts and municipalities. In the programme province of Thanh Hoa visited as part of the ex post evaluation, the FC project was carried out in 7 districts in 32 municipalities. On average, the poverty rate in all municipalities has more than halved, although the official poverty line in rural areas was raised between 1998 and 2006 from an income of VND 70,000 per person per month to VND 200,000. According to information provided by MOLISA and the provincial government, no pro-poor loan programme other than the FC project was carried out. There is thus a clear indication that the FC project has made a contribution to poverty reduction in the programme region. We therefore assess the real economic impact of the project (poverty reduction) as satisfactory.

Indicator (b) could not be implemented. In the context of the ex post evaluation, moreover, no auxiliary indicator could be defined. Overall, the FC project has made a substantial contribution to improving the provision of financial services in the programme region. Access by the target groups to the formal financial sector has been improved. The (statistically not representative) survey of the target groups showed that only some of the borrowers had first-time access to VBARD or other formal financial institutions. The extent to which, in the context of its normal credit business, VBARD will provide a further substantial service to target groups with first-time VBARD loans and without real collateral is open to question. We also evaluate the credit technology in normal use at VBARD as suboptimal for the target group in the FC project. However, we consider positive the fact that the target group (in particular the part of it which previously had no access to the financial sector) was introduced to the formal financial sector and able to gain positive experience of bank financing. In summary, we consider the achievement of the overall objective to be just sufficient.

The programme region comprises the five rural provinces of Thanh Hoa, Ninh Binh, Nam Dinh, Thai Binh and Ha Nam in the north-east of the country in the immediate vicinity of the Red River. The programme target group included those sections of the population in the programme region who live slightly above, on or below the poverty line but who are nevertheless able to make investments that are profitable and eligible for financing. According to our analyses, the programme reached the target group very well. This is indicated by the relatively low average loan, the number of loans granted and the results of the surveys of borrowers conducted during the ex post evaluation.

The project is fundamentally in line with the current development policy objectives and priorities of the federal government in the financial sector (sector concept financial system development from 2003) and in relation to the poverty reduction objectives (MDG). It is also in keeping with the economic and social policy objectives and priorities of the government in Vietnam. Against the background of the long-known challenges of carrying out a fundamental restructuring of the state banks with the aim of improving efficiency, increasing transparency and achieving as much depolitisation as possible, however, future projects with VBARD should be more firmly imbedded in the sectoral reform process. A large number of „small“ projects that are not directly related to sector reforms and are partly under the direct influence of the primarily socio-politically managed MOLISA otherwise run the risk of being counterproductive in terms of VBARD restructuring.

The fact that poor households in the rural regions of the five provinces in the programme have insufficient capital is still a major restrictive factor in terms of generating additional income and diversifying sources of income. In the five programme provinces, the FC project made an important perceptible contribution to giving the target group better access to financial services in the formal banking sector and hence to reducing the restrictive factor. This was achieved, in particular, through the cooperation of VBARD with the Women’s Union. Our analyses show that the positive real economic effects on the target group anticipated in the project appraisal were achieved. At the time of the ex post evaluation a total of 60,136 loans for an average of EUR 198 each (approximately VND 4.1 million) had been granted. The lion's share of the loans were channelled to agriculture, the focus being on animal husbandry. Almost 40% of the borrowers were women. With regard to poverty reduction in the programme provinces, the project made an important contribution to stabilising the economic situation of the borrowers, making it less likely for the target group to slip down to or below the poverty line. The expected impacts on the development of the financial sector (gaining a new client group for VBARD, demonstration effects for other financial institutions and state pro-poor lending programmes) occurred only in part. The ongoing institutional weaknesses of VBARD and the high political resistance, particularly at the local level, to cost-covering and market-oriented interest rates for poor sections of the rural population is hampering the development of the financial sector.

The risks to the achievement of the objectives identified in the project appraisal occurred in that the necessary reforms of SOCB and, particularly, VBARD were implemented more slowly and less consistently than anticipated. This constituted the main weaknesses of the project. However, no foreseeable resultant sustainability risks can be ascertained at present.

In a summarised evaluation of the above mentioned aspects we rate the overall developmental effectiveness of the programme as follows:

<u>Effectiveness</u>

The programme objective was to grant small loans at market conditions to poor rural households. Measured in terms of the objective indicators, the programme objective has only been partly met. A positive assessment is made of the broad impact of the programme, with more than 60,00 loans, a relatively low average loan and the high turnaround rate of the revolving fund with real value retention being nearly achieved. The quality of the FC portfolio, which is probably only just sufficient, can be criticised. However, the actual repayment rate is very high, thanks to the involvement of the Women's Union in the lending process. Ultimate loan losses are relatively rare. The further institutional reforms of VBARD currently being carried out, the apparent increase in the pace of the reform and the generally correct and positive reform orientation are positive signs. We consider particularly positive the progress made by VBARD with regard to greater institutional independence since the programme appraisal. It can be assumed that the Vietnamese state will support the further reform process of VBARD through additionally required recapitalisation measures. Once VBARD has achieved economic independence, further subsidies can probably be stopped or made more transparent. The effectiveness of the project is thus sustained. Overall, we judge the project's effectiveness to be just satisfactory (**sub-rating: 3**).

<u>Relevance/significance</u>

The overall objective was to contribute to poverty reduction in the programme region by giving poor sections of the population better access to financial services. Given the generally positive economic development, the considerable importance of the economically active poor households in the private small and micro business sector and the strong decline in the poverty rate in the programme province of Thanh Hoa, it is feasible to assume that the project will have positive effects on the real economy. The groups targeted by the project were reached effectively. The impact on the real economy (poverty reduction) is unreservedly positive. We consider the impact on the financial sector to be limited. The expected impacts on the development of the financial sector (gaining a new client group for VBARD, demonstration effects for other financial institutions and state pro-poor lending programmes) occurred only in part. However, the revolving of the loan fund can be assumed to lead to a broad-based loan offer for the target groups. Financing loans for economically active poor households is still of basic relevance. Thus, we classify the project's developmental relevance and significance as just sufficient (**sub- rating 3**).

<u>Efficiency</u>

Overall, the earnings situation and the capital endowment of VBARD is slightly insufficient. The same applies to the quality of the portfolio. The indicators of the achievement of the programme objective with regard to the FC portfolio quality have probably not been met. Despite the improvement in the technical opportunities afforded by a real-time management information system, the quality of the data on portfolio quality and loan risk is still poor. We consider the market-based design of the ultimate borrower rates positively. Overall, we judge production efficiency as slightly insufficient. With regard to allocation efficiency, it can be assumed that the rural households make clearly appropriate use of the loans. Overall, we rate the project's efficiency as slightly insufficient (**sub-rating: 4**).

In a summarised assessment of the above impacts and risks we rate the programme as having just sufficient developmental effectiveness **(overall evaluation: rating 3)**.

General conclusions and recommendations

When selecting indicators for the real economic impacts of projects in the financial sector, care must be taken to ensure that reasonable cost and effort is observed in their collection. Moreover, at the time of the project appraisal it is essential to determine the party responsible for any impact analyses which may be required. However, all known empirical methods for an impact analysis ("before and after", comparison with control groups) require a considerable amount of time and cost and generally lead only to very limited results. Therefore, the basic rule should be to give priority either to identifying existing and easily defined real economic indicators (e.g. official poverty rate, number of employees, share of SMSEs in GDP) or to selecting financial proxi-indicatory to illustrate the real economic achievement of the objectives.

It makes little sense to link the real value retention of revolving loan funds in domestic currency to the euro or US dollar as exchange rate developments only rarely reflect inflation differences between the domestic and the foreign economy. By contrast, it is appropriate to take account of the rate of inflation in the partner country (plus any loan losses). The use of appropriate counterpart funds to retain the real value of the revolving fund should be formulated as a standard condition for financial sector projects.

In the case of known structural weaknesses at the project executing agency, such as in the case of VBARD, FC projects should be integrated more firmly into sector projects or at least closely coordinated with them. In so doing, verifiable progress in the restructuring of executing agencies should be taken into account as important conditions/requirements in FC projects.

Assessment criteria

Developmentally successful: Ratings 1 to 3	
Rating 1:	Very high or high degree of developmental efficacy
Rating 2:	Satisfactory developmental efficacy
Rating 3:	Overall sufficient degree of developmental efficacy
Developmental failures: Ratings 4 to 6	
Rating 4:	Overall slightly insufficient degree of developmental efficacy
Rating 5:	Clearly insufficient developmental efficacy
Rating 6:	The project is a total failure.

Performance evaluation criteria

The evaluation of the “developmental efficacy” of a project and its classification during the ex-post evaluation into one of the various levels of success described in more detail below concentrate on the following fundamental questions:

- Have the **project objectives** been achieved to a sufficient degree (project **effectiveness**)?
- Does the project generate sufficient **significant developmental effects** (project **relevance** and **significance** measured by the achievement of the overall development-policy objective defined beforehand and its effects in political, institutional, socio-economic and socio-cultural as well as ecological terms)?
- Are the **funds/expenses that were and are being employed/incurred to reach the objectives appropriate** and how can the project’s microeconomic and macroeconomic impact be measured (aspect of **efficiency** of the project concept)?
- To the extent that undesired **(side) effects** occur, can these be tolerated?

We do not treat **sustainability**, a key aspect to consider when a project is evaluated, as a separate evaluation category, but rather as an element common to all four fundamental questions on project success. A project is sustainable if the project-executing agency and/or the target group are/is able to continue to use the project facilities that have been created for a period of time that is, overall, adequate in economic terms, or to carry on with the project activities independently and generate positive results after the financial, organisational and/or technical support has come to an end.